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April 21, 2004

EX PARTE

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

RECEIVED

APR 21 2004

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Re: Docket No. 96-115

In the Matter of Implementation of the Telecommunications Act of 1996,
Telecommunications Carriers' Use of Customer Proprietary Network Information and
Other Customer Information

Dear Ms. Dortch:

On April 20, 2004, Neg Norton of Yellow Pages Integrated Media Association (YPIMA), Amy Healy of YPIMA, Len Bussey of Verizon Information Services, Mary Henze of BellSouth Corporation (Representing BellSouth Advertising and Publishing Company) and the undersigned met with Jessica Rosenworcel, Legal Advisor to Commissioner Copps, regarding the petitions for reconsideration in the above captioned proceeding. We discussed issues covered in detail in YPIMA's March 19, 2004 ex parte filing in this proceeding. A copy of the attached *Wall Street Journal* article was handed out at the meeting.

Sincerely,



Joel Bernstein

cc: Jessica Rosenworcel

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**Amid High-Tech Turf Battles,
Baby Bells Feel Heat on Cash Cow**

**Mr. Walsh's Yellow Book Pushes
Into \$14 Billion Market
With Cheaper Ad Rates**

By ALMAR LATOUR
Staff Reporter of THE WALL STREET JOURNAL
April 13, 2004; Page A1

KING OF PRUSSIA, Pa. -- Joseph Walsh's face lit up as he compared the Philadelphia yellow pages of rival Verizon Communications Inc. with the city's thicker yellow pages from 1949.

Missing from the today's thinner Verizon book were many of the hairdressers and other small businesses that once considered it essential to be in the yellow pages, he said. "Mom and pop stores can't afford to advertise in directory books anymore."

It's a vacuum that Mr. Walsh, the 41-year-old chief executive of Yellow Book USA, a unit of Yell Group PLC, is working hard to fill. He is riling the once-sleepy yellow-pages industry with a simple formula: selling cheaper ads that attract more advertisers. In just 10 years, Yellow Book, based in Uniondale, N.Y., has grown from a small local directory service to the publisher of more than 500 directories with a total distribution of 72 million in 42 states.

While Wall Street is fixated on the brutal competition to provide phone service, there's an equally brutal competition under way in the \$14 billion yellow-pages industry. As recently as 1995, Baby Bell phone companies and other incumbents snared around 96% of yellow-pages revenue, according to the Kelsey Group, which analyses the industry. Now, they get about 86%.

The Bells badly want to protect this lucrative franchise from further inroads. While yellow-pages advertising accounts for a relatively small part of the revenue for the former Baby Bells, it accounts for a much larger share of their profits. For example, SBC Communications Inc.'s directory services in 2003 made up 10.6% of revenue but 36% of operating income. Losing more of that revenue could make it harder for the Bells to compete in their two biggest businesses: traditional fixed-line phone service and wireless service.

Some of the regional phone companies are slashing yellow-pages ad rates in selected markets, and some have introduced their own cut-rate phone books. The Bells are also making a big bet that much of the yellow-pages business will migrate to the Internet. Verizon, for instance, recently revamped its online listings. Yellow Book also

offers an Internet version of its directory. But Mr. Walsh believes it is premature to invest heavily in this area and that most people will continue to rely on print directories for years.

At the moment, the bulk of the business remains in print. A slew of hungry new entrants have snapped up yellow-pages operations over the past three years as companies such as Qwest Communications International Inc. and Sprint Corp. sold their directory businesses to generate cash. In addition, there are now hundreds of tiny and mid-size directory publishers that compete in smaller cities and rural areas. And there's a growing group of specialized directories catering to Hispanics, Armenians, women, Christians, gays and many other interest groups.

"It's really the birth of a new industry," says George Burnett, the chief executive of Dex Media Inc., Qwest's former directory service, which was bought by the private-equity firms Carlyle Group and Welsh, Carson, Anderson & Stowe last year. "Independence will make us more competitive."



Joseph Walsh

For now, Mr. Walsh's Yellow Book USA appears to be the most ominous threat to the Bells. Through a combination of acquisitions and internal growth, the company's revenue in 2003 hit \$1 billion, compared with \$46 million 10 years ago. Today, three out of four Americans live in a market with Yellow Book directories, and Mr. Walsh aims to push that number higher.

Mr. Walsh has clearly caught Verizon's attention. In January, Verizon filed a lawsuit against Yellow Book, accusing it of unfair sales practices and misleading customers in advertising campaigns and sales pitches.

Pep Rally

At a pep rally last November for Verizon employees in Dallas, Verizon's directory service director showed employees a car covered with the Verizon SuperPages logo and an effigy of Mr. Walsh in the trunk. A lifeless arm with the initials "J.W." dangled outside the trunk. The audience of several hundred Verizon employees cheered when an executive told them "That's where we want Joe Walsh -- in the back seat." A Verizon office in Dallas also has huge custom-made doormats that say "Yellow Book." Employees are encouraged to wipe their feet on the mats upon entering the building.

Verizon spokeswoman Mary Stein says that the company doesn't know of the effigy event. She adds that if it happened, it would have been in the spirit of competition. "Yellow Book is one of many competitors in this industry, and we actually want them all to take a back seat to Verizon," she says.

Mr. Walsh "has been a source of consternation to companies who are not used to competition," says Charles Laughlin, a vice president and yellow-pages expert at Kelsey Group.

Mr. Walsh, who never went to college, got his start as an ad salesman for a tiny service directory in Washington at the age of 19 in 1982. Between pounding on doors, he listened to cassette tapes with lessons of how to do sales pitches in his car. The company went under, but Mr. Walsh had found his calling. He quickly worked his way up from salesman to manager in the directory-service industry.

Sporting pinstripe suits and a boyish haircut, he landed at Yellow Book in 1987. Yellow Book USA had been around since 1930, when it started as a small Long Island community directory. Switching owners numerous times, it ended up in the 1980s as a media company with a hodgepodge of services including voice messaging, beeper reselling and direct-mail coupons.

After being named Yellow Book's CEO in 1992, Mr. Walsh quickly focused the business on directory services, selling off and closing down everything else. At the time, Long Island was reeling from a recession that cost it thousands of jobs. Mr. Walsh decided that he needed to expand so he no longer would depend on a single market.

He envisioned owning 100 small directory books in the Northeast, each a copy of the Long Island operation. He bought a series of small books in New Jersey from publishing giant Gannett Co. in 1996, and as part of the deal acquired two large directory books in upstate New York. It would change the course of the company.

Thinking he would quickly sell the large directories, Mr. Walsh paid a visit to one of their offices in Binghamton, N.Y. The company, based in a converted shoe store, had six sales people who put together a four-color, inch-thick service directory. Mr. Walsh met with some customers, looked at the rival Bell directory, owned by Verizon's predecessor, NYNEX, and then changed his mind. Instead of selling the directories, he would try to turn them around.

He canceled the color ads and switched to black-and-white ones to keep his prices lower for customers. He moved to a three-column format with a bigger font on an 8- by 10-inch page size, from the previous two-column format on a smaller page size. He retrained the sales force. And he moved up the directories' printing date to right before NYNEX's directory came out.

The result: Less than a year after the makeover, the number of ads in the book had increased more than 50% while revenue had shot up 15%, according to Yellow Book. Today, the company runs four books in the Binghamton area with combined revenue of \$4.7 million, up from two books and \$1.25 million in revenue in 1996.

Eager for more money to finance an expansion, Mr. Walsh sold his company to British Telecom in 1999. BT set aside about \$1.8 billion for directory-service acquisitions, and Mr. Walsh snapped up more than 50 small companies in two years. "I was spending the Queen's money to grow Yellow Book," he says.

In 2001, however, British Telecom was forced to spin off its directory-service division to reduce its high debts. The unit was sold to venture capitalists, who put Mr. Walsh in charge of U.S. operations.

With stock as his currency, Mr. Walsh again continued his takeover path, driven to fight the Bells' Yellow Pages, which he calls "the evil empires." In the past two years alone, Mr. Walsh has acquired 40 small directories around the country.

Mr. Walsh said he courted Sandy Goldberg, owner of a small Rockland County, N.Y., directory, for more than four years before he finally persuaded her to sell her company. Just days after the takeover in 2000, Yellow Book threw the directory into what Mr. Walsh calls "the Biosphere" -- a total immersion in the ways of Yellow Book.

Run out of the basement of Ms. Goldberg's home, the directory had a circulation of 100,000 and a staff of four sales clerks. Ms. Goldberg often helped sell ads to local businesses herself and had named the company "Dellwood," a country club to which she belonged.

But under Yellow Book, all that changed. The company gave the directory its own name. It brought in 24 salespeople to reach out to local businesses. Mr. Walsh gave some sales lessons to former Dellwood employees. And it ditched Dellwood's costly red-ink ads, making the book more affordable to small local advertisers.

Four months after the sale, the number of ads in the book had quadrupled, while its revenue had grown to \$2.3 million from \$700,000. Three inches thick, the book competed toe to toe with Verizon's Yellow Pages, the region's dominant directory. "When we arrive in a new community, it's like Pearl Harbor," Mr. Walsh says.

Smaller Customers

It's not just acquisitions that make Yellow Book tick. Mr. Walsh's strategy is to go after smaller customers. Where Verizon charges around \$3,300 for a full-page ad in Philadelphia, Mr. Walsh charges less than \$1,900 for the same. Mr. Walsh says that he can live with Yellow Book's profit margins being a lot lower than those of the Bells' directory services, which can run well in excess of 50%.

Philadelphia dentist Laurence Gordon is an example of a customer Yellow Book has poached. During 20 years, he saw the price of his ads in Verizon's yellow pages climb.

Between 2000 and 2003, Mr. Gordon says the price he paid for ads in Verizon's SuperPages went up roughly 50%, costing him roughly \$1,100 per month last year. "I would always wince a little bit when the bill arrived," says Mr. Gordon, whose dental practice is in the heart of Philadelphia. "It used to be a hefty nut."

So when Yellow Book came along with cheaper rates last fall, Verizon's high prices made it easy for him to

switch Yellow Book offered him ads for about \$400 per month.

So far, Mr. Gordon says, he's getting similar results from the Yellow Book ads, although he wonders how many of his customers are finding him through his old ads in the Verizon yellow pages.

Verizon officials see Yellow Book as just one of many competitors, including local TV, local radio, advertising leaflets and, more recently, the Internet. Lester Chu, vice president for strategy at Verizon Directories, says that smaller advertisers now have many outlets in which they can place their ads. Verizon can command higher fees for ads in its directory books because the books often have higher usage numbers. "It's all based on what advertisers are willing to pay for," says Mr. Chu. "We don't set out to hurt small advertisers." While some Verizon books may be thinner than in the past, Mr. Chu says that's partly because Verizon now has multiple directories for many large cities, including four for the Philadelphia area.

Still, Verizon isn't taking Mr. Walsh lightly. Verizon's lawsuit against Yellow Book, filed in U.S. district court in New York, accuses the company of making "false representations in sales and marketing." Verizon claims that Yellow Book wrongly implies that more people use the Yellow Book than the Verizon SuperPages. In the lawsuit, Verizon also objects to several Yellow Book TV ads, including a January 2004 commercial in which two directories -- Yellow Book and "the Other Book by the phone company" -- are put in a wind tunnel. The Yellow Book resists the wind force, but the other book blows away.

Mr. Walsh dismisses the basic assertion of the lawsuit and says he stands by the ad. "We're confident that we haven't done anything wrong. We're surprised at the action. [Litigation] is not the sort of competition I'm used to."

Yellow Book's offices in King of Prussia, outside Philadelphia, are housed in brown-brick one-story, barrack-like buildings with few decorations. The company's sales force of 3,300 is bigger than that of Verizon's Yellow Pages, even though its current sales are only about a quarter of Verizon's \$4 billion in yellow-pages revenue. Unlike Verizon's sales force of 2,100, Yellow Book agents don't have their own e-mail accounts or laptops. They do get small allowances for cars and cellphones.

In spite of all the rapid growth, Yellow Book still faces significant competition. At a Starbucks outlet in Delaware County, Pa., Dan Staub, a veteran Yellow Book salesman, recently made a sales pitch to a chiropractor who is starting her own practice. He may have been too late. "I am already running an ad in a small upstart women's directory," she explained.